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CONGRESSIONAL OVERSIGHT PANEL

Opening Statement of Ted Kaufman

Congressional Oversight Panel Hearing on Commercial Real Estate

February 4, 2011

Good morning. I am Ted Kaufman, the chairman of the Congressional Oversight Panel for the Troubled Asset Relief Program.

We are here this morning at a pivotal moment in the nation's economic recovery. The financial panic that plagued our country is over. The Dow Jones Industrial Average is nearing its year-end peak from 2007. Housing prices have begun to recover. Private companies are, very slowly, hiring again, beginning to put our millions of unemployed friends and neighbors back to work.

It is only fitting that, as a crisis passes, a government should set aside its crisis authorities, and so Treasury's most extraordinary authority to stabilize our financial system – the Troubled Asset Relief Program – has ended. However, threats to the banking system and the broader economy remain. Our hearing this morning will explore one of those threats in detail: the troubled market for commercial real estate loans.

Commercial mortgages are exactly what they sound like: the loans taken out by developers to buy, build, and maintain commercial properties. Almost everyone who lives in an apartment, works in an office building, or shops at a mall has spent time in a building that owes its existence to a commercial mortgage.

Most commercial mortgages have terms of three to 10 years, but the monthly payments are too low to fully repay the loan in that period. At the end of the term, the entire remaining balance comes due, and the borrower must take out a new loan to finance its continued ownership of the property.

Put another way, a commercial borrower must reapply for credit every few years – and in today's market, where banks remain hesitant to lend and the values of commercial properties have fallen by a third, many borrowers will be turned down. The loans at greatest risk are those made at the peak of the real estate bubble – loans that will come due for refinancing in 2011, 2012, 2013, and beyond. In essence, the term of a commercial loan creates a lag between the moment that the market collapses and the moment that the economic impact is felt. The fuse has been lit, but no one yet knows how much damage will occur when it finally burns down.

The Congressional Oversight Panel has been closely monitoring the commercial real estate market since its first hearing on the subject in May 2009, and the Panel issued a comprehensive report in February 2010. Even after almost two years, the Panel remains deeply concerned. In fact, just last month the missed-payment rate for commercial mortgage-backed securities reached an all-time high of over 9.3 percent.

The commercial real estate market encompasses $3.4 trillion in debt. If borrowers default in large numbers, commercial properties could face a wave of foreclosures. Customers, businesses, and renters in those properties could face uncertainty and even eviction. Small banks in particular could face insolvency, as nearly 1,300 banks nationwide are considered by regulators to have concentrations in commercial real estate.

Concerns about commercial real estate also illuminate a broader theme of our oversight work: that even in a crisis, while authorities must deal with short-term dangers, they must also be vigilant about longer-term threats. If a small bank survived the financial crisis thanks to the TARP but collapses next year due to commercial real estate losses, then TARP support will have served only to postpone the inevitable. Further, more than 500 small banks continue to hold TARP money, and the greater the degree of these banks' exposure to commercial real estate, the lower is the likelihood that taxpayers will recover all of our money.

We are grateful this morning to be joined by two panels of expert witnesses who will help us to explore these concerns, including government regulators and bank analysts. We appreciate your presence and look forward to your testimony.

Let me turn now to Mr. McWatters for his opening remarks.